


TD 93/D115 - Income tax: property development: where net profit is included in assessable income under subsection 25(1) of the Income Tax Assessment Act 1936 -(a) what costs are taken into account in calculating the net profit; and (b) how and when are they taken into account?

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Draft Taxation Determination

Income tax: property development: where net profit is included in assessable income under subsection 25(1) of the *Income Tax Assessment Act 1936* -

- (a) what costs are taken into account in calculating the net profit; and**
- (b) how and when are they taken into account?**

1. Only costs that otherwise would be deductible under the statutory provisions relating to allowable deductions (together with the value of the property at the date it was committed to the business operations) are taken into account.
2. They are not deductible as they are incurred. Instead, such costs are subtracted from the gross proceeds of sale to determine the net profit to be included in assessable income in the year in which the property is disposed of.
3. This is because the net profit basis of returning income is a departure from the statutory scheme of subtracting allowable deductions from gross income: see comments of Mason J in *FC of T v. Whitfords Beach Pty Ltd* 82 ATC 4031 at 4040; (1982) 12 ATR 692 at 702; and in *Commercial and General Acceptance Limited v FC of T* 77 ATC 4375 at 4380; (1977) 7 ATR 716 at 721.
4. The view that only those costs otherwise deductible under the statutory provisions are taken into account is supported by the remarks of Mason J in the *Commercial and General Acceptance Limited (CAGA)* case at 4380 to the effect that the inclusion of net profit as assessable income can be reconciled with subsection 51(1) notwithstanding that the calculation does not involve the application of 51(1): see also his Honour's comments in the *Whitfords Beach* case at 4046.
5. His Honour's remarks in *CAGA* and *Whitfords Beach* indicate that costs which generally would not be allowable under the statutory provisions cannot be subtracted from the gross proceeds of sale in order to calculate the net profit which is included as income under subsection 25(1).
6. Where the land is subdivided and sold, the value of the land and costs of subdividing and developing it must be apportioned in respect of each allotment. The net profit on the sale of each allotment is included in assessable income in the year of income in which it is disposed of.

Example:

In the year of income ending 30 June 19X1, a taxpayer enters into an isolated business venture involving the subdivision, development and sale of land which was not acquired originally by the taxpayer for that purpose. In the year ending 30 June 19X3, the taxpayer commences to sell allotments.

During the course of subdividing and developing the land, the taxpayer incurs the following costs: architects' fees, engineers' fees, planning approval fees, interest on money borrowed to meet the costs of development, charges for hire of plant and machinery to undertake development work, advertising and marketing fees, entertainment expenses, traffic fines. The taxpayer also creates provisions for bad debts and long service leave.

The architects' fees, engineers' fees, planning approval fees, interest, hiring charges, and advertising and marketing fees are apportioned in respect of each allotment in order to calculate the net profit to be included in the taxpayer's assessable income in the year in which an allotment is sold. On the other hand, the entertainment expenses, traffic fines and provisions for bad debts and long service leave are not deductible under the statutory provisions, and they cannot be taken into account in calculating net profit.

Commissioner of Taxation

13/5/93

FOI INDEX DETAIL: Reference No.

Related Determinations:

Related Rulings:

Subject Ref: property development; assessable income; isolated business venture; net profit; allowable deductions

Legislative Ref: ITAA 51(1)

Case Ref: *FC of T v. Whitfords Beach Pty Ltd* 82 ATC 4031, (1982) 12 ATR 692; *Commercial and General Acceptance Limited v. FC of T* 77 ATC 4375, (1977) 7 ATR 716

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